UNDERWRITING GUIDELINES & FINANCING POLICY

Multifamily Programs and Lending
(Construction and/or Permanent)

Please Take Notice

These underwriting guidelines, policies, procedures, and forms may be amended from time to time due to changes in market conditions and/or changes in the HMFA's housing policies or initiatives. Such amendments may occur without notice and are applicable to all pending and future applications. Applicants are, therefore, responsible for contacting the HMFA to ascertain whether or not there have been any changes since the date of these guidelines and for complying with such changes.

Eligible Sponsors/ Borrowers

Qualified housing sponsors are defined as qualified for-profit and non-profit housing sponsors, preferably with experience in providing housing; or, associations of persons organized under the New Jersey Statutes; or any corporation having for one of its purposes the improvement of realistic opportunities for low- and moderate-income housing, and appearing capable, by virtue of past activities, qualifications of staff or board, or other features, to develop and operate housing projects.

Sponsoring entity must be formed for the sole purpose of owning and operating the project and shall own no other assets unrelated to the project.

NOTE: HMFA will not consider any new/additional financings to developers/sponsors or their principals who currently have an outstanding HMFA mortgage loan(s) and who: (1) are more than twelve (12) months delinquent on said mortgage loans(s) unless the developer/sponsor develops and provides a workout plan that is acceptable to the HMFA Executive Director and Chief Financing Officer and is compliant therewith, or (2) have been served with a notice of default, monetary or otherwise pursuant to the mortgage loan documents, unless and until (a) such default has been cured by the developer/sponsor to the satisfaction of the Executive Director or, if applicable, the HMFA Board, or (b) developer/sponsor develops and provides a workout plan that is acceptable to the HMFA Executive Director and Chief Financing Officer or, if applicable, the HMFA Board, and is compliant therewith.

Nothing in the foregoing is intended to limit the rights of the Agency to exercise its remedies under the mortgage loan documents at any time.

Types of Rental Housing	**Family, Senior, Preservation, Supported Housing and Special Needs.**
Loan Options	**Construction only, Construction and Permanent and Permanent only.**
Types of Financing Structures	**Tax exempt financing, Taxable financing, Mixed use and Mixed income**

Eligible Projects

The Sponsor must obtain a resolution from the municipality in which the project will be located reciting that there is a need for the particular housing project in that municipality.

"Scattered site project" means a project that consists of buildings which are not all proximate to one another but located within the same municipality. The entire project must be included within a municipally approved redevelopment area. The Agency must determine that a scattered site project would be a compliment to the municipality's overall redevelopment plan. A project that is complementary to an overall redevelopment plan will be found to have a positive impact on the neighborhood by improving the health, safety and welfare of the residents. To be considered an eligible project, each building must meet one or both of the following criteria: (1) be within ½ mile of a rail, light rail, subway, ferry, or major bus corridor station (2) within an approximate ½ mile radius of the most central project building. Additionally, each building must be underwritten as self supporting and the developer will be responsible for providing personal guarantees or other acceptable credit enhancement on each building as security against the aggregate loan. The developer must also demonstrate that management and operations of these scattered properties is possible and efficient.

Tax Abatement

The developer should obtain a municipal resolution granting a real estate tax abatement and authorizing an agreement for payments in lieu of taxes ("P.I.L.O.T.") for the project under the HMFA's statute, N.J.S.A. 55:14K-37, during the mortgage term. Furthermore, it is beneficial to the project if a tax abatement is obtained pursuant to the HMFA's statute rather than the Long Term Tax Exemption Statute.

In general, the HMFA has found that a project without a tax abatement or a project with a tax abatement under the Long Term Tax Exemption statute has trouble demonstrating financial feasibility. Lack of a tax abatement pursuant to the HMFA's statute may raise the risk to the HMFA and therefore may require additional security in the form of increased debt service coverage and/or the escrow of additional funds.

Financing Options

Tax Exempt Bonds

Projects using tax-exempt financing are subject to restrictions under the Internal Revenue Code, which requires that either a minimum of 20% of the units must be occupied by persons earning 50% or less of median income or a minimum of 40% of the units must be occupied by persons earning 60% or less of median income.

Tax Exempt Rules for Residential Rental Property

Section 142(d) of the IRS code and the applicable regulations there under defines a residential rental project as a building or structure, together with any functional related and subordinate facilities, containing one or more similarly constructed units which (i) are to be used on other than a transient basis, (ii) are available to the general public and (iii) satisfy the continuous rental and low or moderate income occupancy requirements. Hotels, motels, dormitories, fraternity and sorority houses, rooming houses, hospitals, nursing homes, retirement homes, sanitariums, rest homes, and trailer parks are not residential rental projects.

A residential project should also be composed of qualifying units, together with facilities functionally related and subordinate thereto. Buildings and structures which have similar constructed units are treated as part of the same residential rental project if they are in proximity to one another (located on a parcel or parcels of land which are contiguous except for the interposition of a road, street, stream or similar property), are owned by the same person for Federal tax purposes, and are financed pursuant to a common plan (i.e., by bonds issued under the same indenture).

Tax Exempt Rules for Complete Living Units

Section 142(d) of the IRS code and the applicable regulations there under defines a complete unit as any accommodation containing separate and complete facilities for living, sleeping, eating, cooking and sanitation, which may be served by centrally located equipment such as air conditioning or heating. The Regulations provide as an example of a “unit” an apartment containing a living area, a sleeping area, bath and sanitation facilities, and cooking facilities equipped with a cooking range, refrigerator and sink, all separate and apart from other apartments.

Tax Exempt Bonds Volume Cap Tax Credit

The HMFA may finance projects utilizing tax-exempt bonds with the intention of being eligible for credits on 100% of the projects’ eligible basis by satisfying the requirements established by the Internal Revenue Service 50% (the HMFA uses 55% as a safe harbor) of aggregate basis test.

Meeting the 55% test is often achieved through the provision of two first mortgage notes. The first note is sized based upon the amount of debt that can be amortized in accordance with the HMFA's underwriting standards. The second note is sized based upon the difference between the first note and that amount of funding needed to achieve 55% coverage of the aggregate costs. The sponsor must demonstrate a source of funds to pay off the second note, which must be collateralized in a form satisfactory to the HMFA. The determination that a project meets the 55% test and the term of the debt to be retired is subject to HMFA bond counsel opinion.

See Typical HMFA Fee and Transaction Cost section.

Taxable Bonds

The HMFA can issue bonds that are not exempt from federal taxation and utilize the proceeds to fund mortgages.

Maximum Loan Amount

For non-profit developers, the maximum loan amount may not exceed the lesser of (a) 100% of the total project costs, (b) the amount that can be amortized by the project, as determined by the HMFA.

For profit-motivated developers, the maximum loan amount may not exceed the lesser of (a) 90% of the total project costs, (b) the actual appraised value at completion and/or (c) the amount that can be amortized by the project, as determined by the HMFA. The 90/10 ratio of loan amount to project cost must be maintained on a cumulative basis for each construction draw when using HMFA construction financing.

For all loans, whether to non-profit or profit-motivated developers, the HMFA reserves the right to set the actual loan amount in accordance with the HMFA's overall program goals, and determination of acceptable risk. Accordingly, the actual loan amount may be less than the maximum amount permitted above.

In no event shall the sum of HMFA's total mortgage financing, inclusive of subordinate HMFA mortgages, exceed the "as completed" appraised value.

HMFA Subordinate Loans

The aggregate of HMFA's first and subordinate loan amounts may not exceed the "as completed" appraised value.

Debt Service Coverage Ratio

The debt service coverage ratio is the relative cash flow available to meet the annual interest, principal and HMFA servicing fee payments on debt. A project's cash flow analysis must achieve and maintain a projected minimum debt service coverage ratio of 1.15 for the initial 15 years of the loan to be eligible for financing. The establishment of an Operating Deficit Escrow Account (ODEA) account may be required if a project negatively trends below a 1.15 debt service coverage ratio for the term of the mortgage.

Debt Service Coverage Ratio Calculation is as follows:

$$\frac{\text{Net Operating Income}}{\text{Agency Debt Service + Servicing Fee*}} = \text{Debt Service Coverage Ratio}$$

*See servicing fee at Typical HMFA Fee and Transaction Cost

Risk Analysis

Projects with expiring rental assistance or rental assistance subject to annual appropriations and/or funding approvals may be under written subject, but not limited, to the following assumptions:

- Flat rental income subsidy stream for the term of the mortgage;
- Shorter mortgage term coterminous with the expiring rental assistance;.
- Fully funded Operating Deficit Escrow Account; and/or
- Another form of insurance acceptable to HMFA underwriting staff.

Projects may also be subject to additional credit enhancement obligations based upon the HMFA's assessment of the associated risk involved in providing a mortgage for construction only, construction and permanent or permanent only financing. Such enhancement obligations may include but are not limited to mortgage insurance, recourse loans, an operating deficit reserve account, permanent take out after the project has reached 95% occupancy and sustainability over a 6 month period, an increase in debt coverage ratio, a guaranty of the principal owner of the project's ownership entity for repayment of the Agency financing and/or any other credit enhancement that may be deemed acceptable to Agency underwriting staff.

In addition to the aforementioned enhancements, HMFA may recommend that developers, with little or no experience in housing development and/or with the HMFA, should partner with a successful developer that has developed and operated at least two other developments of similar size and scope to the subject development. Successful developers are defined but are not limited to, (1) those that have completed projects on time and on budget with no outstanding issues, (2) being current with debt service payment obligations, (3) being in good standing with federal, State and municipal governments, (4) having no issues of non-compliance housing issues of any kind and (5) those that have completed projects that are occupied and sustainable and are maintaining an acceptable debt service coverage ratio for six consecutive months as of the submission of application to HMFA.

If the HMFA is providing construction financing, HMFA will add an additional 6 months to the construction term and may require experienced general contractors only. Experienced general contractors are defined, but not limited to: 1) having successfully completed at least two other projects similar in size and scope 2) completing the projects on time and on budget 3) being in good standing with federal, state and municipal government and the Better Business Bureau 4) having no issues of non-compliance of any kind.

Term

Standard term is 30 years. Developers may request a term of less than 30 years or may request a term of more than 30 years; however, the Agency reserves the right to request mortgage insurance and/or credit enhancements upon HMFA's assessment associated with the risk of providing a mortgage in excess of 30 years.

Lien Status

All loans will be secured by a first mortgage lien on the land and improvements if the borrower owns both in fee simple. If the borrower occupies the property pursuant to a ground lease, the HMFA will require a first leasehold mortgage secured by the borrower's interest in the lease and the improvements; The term of the ground lease must at a minimum be for the term of the Agency's first mortgage, and affordability restrictions and be in all respects satisfactory to the HMFA. To further protect the Agency's interests, the parties shall enter into a non-disturbance agreement with the HMFA wherein the lessor will promise, among other things, not to terminate the ground lease during the term of the Agency's mortgage(s) and affordability restrictions except by reason of default of the borrower, and in no event without first giving the Agency notice and opportunity to cure that default, and, if required by the HMFA and/or the Attorney General's Office, amending the ground lease when curing a default by the borrower.
An additional processing and review fee will be charged at time of application, to any project sponsor, which seeks Agency financing to be secured by a leasehold mortgage.

See Typical HMFA Fee and Transaction Cost section.

The form and substance of the non-disturbance agreement must be acceptable to the HMFA and the Attorney General's Office.

Junior Financing

The HMFA may permit junior financing. This financing may be in the form of an amortizing loan, subject to HMFA consent, provided the project is able to maintain a minimum of a 1.15 debt service coverage ratio including the junior financing. The junior financing may not cause an acceleration of the HMFA's first mortgage loan unless approved by HMFA.

Security/Collateral

HMFA loans are secured or collateralized by a lien on the land, improvements, project revenues and escrows. There is generally no recourse to other assets of the borrower except in the case of fraud or other acts with regard to the project.

Mortgage Interest Rate

The mortgage interest rate is a fixed rate for the term of the mortgage and will be determined based upon the HMFA's actual cost of funds and allowable spread. The rate will be locked at the earlier of execution of rate lock, loan closing or one week prior to bond pricing. For current rates you may call the Multifamily Programs Division or visit our web site at www.state.nj.us/dca/hmfa/biz/devel/multi/interest.html.

The rate is locked one week prior to the pricing of bonds that will fund the loan and will be fixed for the term of the loan assuming no rate lock is executed and project has not closed, developers are responsible for the interest rate risk prior to that period as the positive or negative change in the interest rate will have the effect of increasing or decreasing the mortgage that the project can support and remain in compliance with the HMFA's Underwriting criteria.

Commitment Term

Construction and permanent loan commitments will expire 90 days after the anticipated construction start date. In the case of permanent only loans, the commitment will expire 90 days after the anticipated construction completion date. The Executive Director is authorized to extend the commitment for two additional consecutive 90-day periods, if deemed appropriate in their sole discretion. A written request for extensions must be made.

Determination of Project Cost

Subject to the maximum loan amounts set forth above, the HMFA may finance project costs as determined by the HMFA and as defined in NJSA 55:14K-3q. The HMFA is required to determine that all costs are reasonable or necessary. The HMFA will require the Developer to submit an audit of projects costs.

Return on Investment The HMFA limits the return on investment that the owners receive annually and upon sale of a project, pursuant to N.J.A.C. 5:80-3. The base amount of the investment will be determined after the project costs are audited and thereafter periodically adjusted. The return on the base amount of the investment will be determined by, the percentage of low (50% of median and below), moderate (50% to 80% of median) and market rate units in the project. The following rates of return shall apply. The base rate is the 30-year Treasury bond rate at the time of the mortgage closing.

Base rate + 6% for percentage of low-income units
Base rate + 4% for percentage of moderate-income units
Base rate + 2% for percentage of market rate units

Sale or Prepayment The HMFA prohibits the sale of the project or any interest therein without prior HMFA approval. Secondary financing, representing a portion of the purchase price of the project or interest therein, may be permitted by the HMFA as set forth in its regulations at N.J.A.C. 5:80—5.7. Such secondary financing shall be subject to the HMFA's standard underwriting analysis to determine its impact on project financial feasibility and affordability requirements. In performing its underwriting analysis, the HMFA will take into account any potential non-renewal of or non-appropriation for any governmental subsidies to the project, including, but not necessarily limited to, project-based Section 8. If the project's mortgage term exceeds 20 years, it may be prepaid after year 20; however, the low-income housing and other HMFA restrictions remain in place through the original mortgage term pursuant to N.J.A.C. 5:80-5.10.

Tax Credits All tax credit projects will need to comply with all tax credit rules and fulfill the requirements of their tax credit reservations and allocation. Projects receiving HMFA financing are not subject to the annual tax credit-monitoring fee.

Underwriting Analysis

Site Acceptance The HMFA will visit the site to determine that the site is suitable for the development's purpose.

Real Estate Valuation The HMFA recognizes the lesser of the appraised value or the purchase price or lease fee of the realty and any buildings and improvements thereon, in the most recent arm's length transaction as provided by a "Delineation of Title" history (completed by the appraiser) identifying each party associated with the conveyance for a maximum of 10 years. The appraised value of the real estate may be considered if the arms length transaction exceeds 10 years.

The total purchase price may include documented carrying costs, expenditures to obtain zoning, environmental or other governmental approvals necessary or useful for the development of the project, and the costs of improvements erected for the benefit of the project. The difference between the actual purchase price or lease fee and the appraised value, if the purchase price or lease fee is higher, may be recognized for the purpose of Return on Investment.
NOTE: Arms Length Transaction is defined as: A transaction negotiated by unrelated parties, each acting in their own self interest in arriving at a basis for a fair market value determination.

Appraisals

An independent appraisal, which conforms to the Uniform Standards of Professional Appraisal Practice (USPAP) and in accordance with the HMFA standards, will be commissioned by the HMFA to determine project valuation for both the site and building. Where applicable, the value of the federal low income housing tax credit must be provided. Regardless of whether or not the project has received a tax abatement, the appraisal will also provide the most recent tax assessment on the property. The cost of the appraisal will be passed through to the developer.

See Typical HMFA Fee and Transaction Cost section

NOTE: While the cost of the appraisal is borne by the developer/sponsor, the HMFA will order the appraisal. The process is as follows:

- An appraiser is selected from a computer database that keeps a rotating list of appraisers that have been pre-approved to do business with the HMFA. The appraiser at the top of the list is selected based on the type, size and location of the project to be appraised.
- If for some reason, the selected appraiser cannot complete the requested appraisal, the computer will then provide three alternates. The HMFA will request a bid from those three appraisers and select a qualified bidder to do the required work.
- Once a price has been given and accepted by the HMFA, the developer/sponsor is notified of the cost. At that time, the developer/sponsor is required to send a check for that amount to the HMFA. **<u>No</u> appraiser will be authorized to begin work until the HMFA has received the check.**
- The developer/sponsor is responsible for providing all information to the Credit Officer that is needed for the

appraiser to complete the assignment. **<u>In turn, the Credit Officer will provide that information to the appraiser.</u>**

- **<u>The developer/sponsor is to have no contact with the appraiser</u>** and **<u>the appraiser is to have no contact with the developer/sponsor until the appraisal has been completed, reviewed by staff and approved.</u>**
- Once the appraisal has been approved by the HMFA, the developer/sponsor will be supplied with a copy of the appraisal.

(See Appraisal Standards. For a copy contact the Multifamily Programs and Credit Division at 609-278-7519.)

Appraisal Updates

All appraisals have a shelf life. Property Values change quickly and are dependent on many different data. The demographics change, as do economic indicators. A supply and demand study can be affected by new construction or a change in purpose. For this and other due diligent reasons, the HMFA requires that appraisals be updated under the following circumstances.

- An appraisal completed for a project that involves New Construction is valid for one year (12 months) after the time of commitment. All commitments for permanent financing of projects involving new construction will be conditioned upon an updated or new appraisal at the time of commitment expiration. The HMFA will assess the time remaining for completion of the project and make a determination as to whether an update or new appraisal will be ordered. An exception to this requirement will be for any loan closing within a 30-day window of the appraisal expiration date.
- An up-date must be ordered if the appraisal is in a Bond issue and the appraisal age exceeds that required by the bond underwriter (6-12 months). The multifamily division will assess the actual appraisal and the risk to the Agency for each individual project. Some of the determining factors to be used to determine when the appraisal should be up-dated are LTV, market area stability and rental structure, project type and status, etc.
- An up-date must be ordered if the appraisal is more than 6 months old and a re-commitment is needed. Again, the multifamily division will assess the actual appraisal and the risk to the Agency for each individual project. Some of the determining factors to be used to determine when the appraisal should be up-dated are LTV, market area stability and rental structure, project type and comparables, etc. This applies even if Bonds have been sold.

NOTE: An appraisal can only be updated two times before a new appraisal should be ordered. Additionally, once an acquisition value has been set by the first appraisal, that “as is” value or Purchase Price (whichever is less) has been determined and will not change.

Market Study*

A market study or a supply and demand analysis is generally included in the appraisal. Under certain circumstances, the HMFA may require a more detailed market study to determine the overall vacancy rates, absorption periods, penetration rates, rental comparable, marketing plan, and budget. The HMFA will order the study. The cost will be passed through to the Developer.
(Also see Typical HMFA Fee and Transaction Cost section)

* If at the time of bond sale or recommitment the appraisal and/or market study report are more than 6 months old, an update will be ordered and the cost will be passed on to the sponsor. The reports should demonstrate, to the satisfaction of the HMFA, that the appraised value of the project still meets the HMFA’s underwriting requirements and that the rent-up and/or operational feasibility of the project has not been compromised. If the updated appraisal and/or market study demonstrates that the appraised value is reduced or the rent-up and/or operational feasibility of the project has been compromised, the HMFA is not required to extend the mortgage commitment, include the project in its bond sale and/or make the permanent loan. If the HMFA extends the mortgage commitment, and/or includes the project in its bond sale, the HMFA may adjust the amount of its mortgage loan and the other terms and conditions of its commitment, as it deems necessary to address changes arising from the updated appraisal and/or market study.

Marketing Plan

For all projects receiving an HMFA commitment, the sponsor and/or the managing agent must provide a marketing plan for the HMFA's approval and acceptance. This plan must outline all the preliminary marketing to be accomplished prior to opening and thereafter. The plan must also provide for the on-going marketing efforts that will be made to keep the project fully occupied. The outline must provide a time line for all anticipated activities and should be tied to benchmarks during construction.

Where the HMFA is making both the construction and permanent loan, the plan must be submitted prior to closing on the construction loan. Where the HMFA is providing only the take-out financing, the project must submit its marketing plan prior to construction start. In certain cases of rehabilitation where there is an existing occupancy, the sponsor and/or the managing agent should submit documentation that a full marketing plan is not needed and give the reasons the HMFA should accept a lesser marketing analysis.

Once construction has begun, monthly progress reports should be provided to the Director of the Property Management Division of the HMFA or his designee.

Physical Needs Assessment

For Preservation projects, a Physical Needs Assessment may be required to provide an estimated cost and scope of work needed to address major systems, including but not limited to; elevators, roofs, HVAC, electrical, plumbing, security, energy efficiency, windows. The Assessment should be conducted within 12 months of commitment in accordance with HUD's Electronic Green Physical Needs Assessment Tool or other format acceptable to the HMFA. The Assesment should address the following items:

1. Those items in need of immediate repair or replacement.
2. Those items in need of repair or replacement within a 12-month period.
3. Those items that will need repair, replacement or significant maintenance over the term of the mortgage.
4. Determine the rehabilitation escrow and repair and replacement account requirement.

Building Design

The HMFA discourages the use of EIFS (Exterior Insulation Finish Systems such as DRYVIT) and electric heating systems. If the use of either of these systems is contemplated, it must be disclosed at the application stage and written authorization received from the HMFA before engaging professionals to produce Design Development drawings.

Unit Standards for gut rehabilitation and new construction units only:

For the most part, HMFA does not dictate the design of the project; however it has set minimum unit sizes for gut rehabilitation and new construction. If the minimum unit sizes cannot be met, justification must be provided and a market study will be required to evaluate the marketability of the smaller units compared to the comparables in the study. In addition, possible solutions to accept smaller units may include, but may not be limited to discounting the rents, increasing the working capital reserve account, etc….

The sizes listed below are minimums only. Measurements are taken from the inside faces of the perimeter walls of the units.

Minimum unit sizes:

Efficiency/Studio Units – minimum of 550 sq. ft.
One-Bedroom Units – minimum of 600 sq. ft.
Two-Bedroom Units – minimum of 850 sq. ft.

Three-Bedroom Units – minimum 1,150 sq. ft.
Four-Bedroom Units – minimum 1,250 sq. ft.

NOTE:
<u>In addition, units with three bedrooms or more must have at least 1 ½ bathrooms.</u>

Developers are encouraged to make developments as energy efficient as possible by utilizing the standards provided within the DOE/EPA's ENERGY STAR program and to review the current 'Guide to NJHMFA ENERGY STAR Requirements' for more options. In addition, the NJHMFA strongly supports projects that incorporate "green" building concepts; categorized as energy efficiency, renewable energy, and green building. For more information, please contact the NJ Green Homes Office, located within NJHMFA, and found at www.njgreen.gov.

Developers are also encouraged to install individual metering with direct billing by the utility provider for gas and electric for all new construction projects, all gut and substantial rehabilitation of unoccupied buildings, and all conversions or adaptive reuse of existing structures. Master metering is also permitted, but individual metering is encouraged. NOTE: *NJ ENERGY STAR Homes requires that at least one utility (electric or gas) be individually metered.*

Submetering of gas, electric and/or water and sewer is specifically prohibited for all new construction, all gut and substantial rehabilitation of unoccupied buildings and all conversions or adaptive reuse of existing structures.

For **substantial (gut) rehabilitation projects**, a structural engineering report on the existing structure, acceptable to the HMFA, must be submitted. All existing mechanical, plumbing and electric systems must be replaced.

If the degree of rehabilitation to be accomplished is **less than substantial**, an engineer's report describing the condition of these building systems, and listing their recommendations, must be submitted. The HMFA's **GUIDELINES AND CHECKLIST FOR ASSESSING EXISTING BUILDING SYSTEMS** describes issues and offers recommendations to follow in preparing this report.

In all **multi-story** buildings that contain an elevator, a trash chute and compactor are to be installed.

In **aged restricted buildings** the following items are to be installed:

Emergency pull cords in bathrooms and bedrooms

A grab bar to facilitate entering and exiting a bathtub or shower

Handrails on both sides of common corridors

An emergency generator serving common areas and elevators

Construction Budget

The construction budget must be supported by a Summary Trade Payment Breakdown signed by the contractor. This document and other supporting schedules such as the construction completion schedule and design development drawings must be submitted by the contractor and approved by the Director of Technical Services. Refer to the Technical Services Requirements attached to the Document Checklist, for the timing of the submission of these documents.

Wage Rates

If the HMFA is providing construction financing, the contractor and subcontractors must pay prevailing wages as determined by the N.J. Department of Labor except that prevailing wages determined by the U.S. Department of Labor under the Davis Bacon Act shall be used if the HMFA construction loan is subject to direct or indirect federal assistance.

Sales Tax Exemption

Sales of materials or supplies to housing sponsors utilizing HMFA construction financing are exempt from NJ State sales tax. Sales of materials or supplies to contractors for the purpose of erecting housing projects which have received HMFA construction financing and other local, state or federal subsidies are exempt from NJ State sales tax.

Environmental Review

The HMFA requires the submission of a Phase I Environmental Assessment and a Phase II Environmental Assessment should the Phase I call for further investigations.

Should remediation be recommended, a Preliminary Assessment Report as described in N.J.A.C. 7:26E-3.2 is required. Additional assessments, such as a Site Investigation described in N.J.A.C. 7:26E-3.3 et seq., or DEP environmental remediation measures may also be warranted. Rehabilitation projects must provide a plan for asbestos removal and remediation of lead-based paint and radon. A letter of "no further action" from DEP may be required.

A transaction update from the consultant, indicating that no further pollutants have been introduced to the site, will be required on all assessments or investigations prepared more than six months prior to construction start.

Professional Liability Insurance*

Contractor

- General liability
- Worker’s compensation
- Contractor's public liability in the sum of $1,000,000/$3,000,000 and property insurance of $250,000/$500,000

Architect

- Architects must have Errors & Omission Insurance of 10% of the construction costs or $250,000, whichever is greater.

*All insurance must be issued by a firm with an A.M. Best Rating of A- VII or better acceptable reinsurance.

General Liability Insurance*

All insurance must be issued in accordance with New Jersey Housing and Mortgage Finance Agency Insurance Specifications Minimum Requirements effective April 1, 2006 as may be amended from time to time.

*All insurance must be issued by a firm with an A.M. Best Rating of A- VII or better with acceptable reinsurance.

Construction Completion Guarantees

Construction and Permanent Financing*

Where the HMFA provides the construction and permanent financing, a 100% Payment and Performance Bond is required for a term from the HMFA loan closing date through 2 years from the date of issuance of the Certificate of Occupancy or Architect’s Certification of Substantial Completion, whichever is the latter.

Permanent Financing*

Where HMFA construction financing is not used, the developer must provide one of the following for a term of 2 years from the date of issuance of the Certificate of Occupancy or Architect’s Certification of Substantial Completion, whichever is the latter:

-100% Payment & Performance Bond equal to the construction cost.
-Letter of Credit equal to 10% of the construction cost.
-Warranty Bond equal to 30% of construction cost.

*All bonding companies must be rated with an A.M. Best Rating of B+ or better.

Construction Contingency The contingency may be used to cover increases in both hard and soft costs.

The budgeted contingency for new construction projects must be at a minimum of 5% of the construction costs.

The contingency for rehabilitation projects must be at a minimum of 10% of the construction costs. This may be adjusted based upon an acceptable engineering report submitted to the HMFA.

In all cases, the budgeted contingency for soft costs must be at a minimum of 1% of the budgeted expenses.

Developer's Fee The amount of the developer fee allowed for eligible rehabilitation or new construction costs is limited to 15.00 percent of total development cost excluding acquisition (that is land and building), working capital, marketing expenses, escrows, operating deficit reserves, step-in-the-shoes costs and costs associated with syndication as determined by HMFA. However, a developer fee of up to 20.00 percent (of total development costs excluding acquisition, working capital, marketing expenses, escrows, operating deficit reserves, step-in-the-shoes costs and costs associated with syndication) is allowed for 1) scattered sites single-family detached or duplex housing 2) projects of 25 units or less or 3) Supportive Housing Cycle projects.

In addition, the non-deferred portion of the developer fee for all projects shall not exceed 8.00 (13.00 percent for the three types of housing referenced 1, 2 and 3 above) of the total development cost excluding acquisition, working capital, marketing expenses, escrows, operating deficit reserves, step-in-the-shoes costs and costs associated with syndication. The deferred portion of the developer fee shall be achieved from cash flow by way of Return on Equity after payment of debt service, operating expenses and funding of all required escrows and reserves.

A developer fee of up to 8.00 percent shall be permitted for building acquisition costs; however, the non-deferred amount of this portion of the developer fee shall not exceed 4.00 percent of the acquisition amount.

The developer fee does not include fees paid to the architect, engineer, lawyer, accountant, surveyor, appraiser, professional planner, historical consultant, and environmental consultant. Executed contracts for these professionals shall be submitted to the HMFA before being recognized as a separate line item expense. Certain fees are subsumed within the developer fee – such as acquisition fees, compensation to the general partner, financial consultants, employees of the developer, construction managers/monitors, clerk of the works and syndicator-required consultants.

Developers may pledge their fee toward meeting the equity requirement. The amount allowable will be determined at the sole discretion of the HMFA. **The developer's fee is earned on a pro-rata basis during the construction period based upon the percentage of construction completion. The unpledged portion of the developer's fee is payable only when earned and is earned only after the entire pledged portion has been earned.**

Working Capital

Working capital is funded at the time of construction and/or permanent loan closing and is generally used to cover necessary operating expenses, debt service and HMFA fees until the project has reached sustaining occupancy for a period of six months. For more information, refer to the Working Capital Funds Policy #5006 in the Management Policies and Procedure Manual. The formula for computing working capital is as follows:

$$\frac{\text{Operating Exp + Debt Service + Agency Fee x 75\%}}{12} \ \mathbf{X} \ \text{\# of months of rent}$$

Operating Expenses

For current minimum you may visit our web site at: http://www.state.nj.us/dca/hmfa/media/download/multi/mf_operating_expenses.pdf

Vacancy Rate

The vacancy rate used for each project will be determined by the market study and appraisal. At initial application, a minimum of 5% vacancy rate may be used.

Escrow Requirements

The escrows listed below must be funded from the capital budget at the time of closing on the initial Agency loan whether a construction and/or permanent loan and must remain in place for the term of the mortgage.

*Insurance -	one-half year's hazard insurance premium
*Taxes-	one-quarter of taxes - this may be on real property and/or a payment in lieu of taxes
Debt Service -	one-month's principal, interest and servicing fee payment.
Risk Share Premium -	one- year's insurance premium plus one-quarter of the following year's premium (if applicable).
Other Credit Enhancements-	as per program requirements

* Additional escrows may be required at closing for the Agency to make the next payment or renewal.

Income Targeting

(All units are subject to income targeting)

Low and Moderate For marketing purposes the HMFA will underwrite low and moderate-income rents at 47.5% of median income and 57.5% of median income, respectively.

Market Rate At initial occupancy, the gross aggregate family income of the tenants in each unit may not exceed six times the annual rent or carrying charges, including the value or cost to them of heat, light, water, sewer, parking facilities, and cooking fuel or seven times those charges for tenants with three or more dependents.

Rents The restrictions on tenant income and on rents shall be enforced through a deed restriction on the project and land for the term of the HMFA's mortgage. Projects receiving tax credits shall also be subject to a deed restriction pursuant to the Internal Revenue Code.

Please be advised that, according to Section 807 (b)(2) of the Federal Housing Act, "housing for older persons" must meet one of the following categories:

(A) provided under any State or Federal program that the Secretary determines is specifically designed and operated to assist elderly persons (as defined in the State or Federal program); or

(B) intended for, and solely occupied by, persons 62 years of age or older (100% of the individuals living in the building must be age 62 or older); or

(C) intended and operated for occupancy by persons 55 years of age or older; or

- (i) at least 80 percent of the occupied units are occupied by at least one person who is 55 years of age or older; <u>20% can be non-age restricted</u>;
- (ii) the housing facility or community publishes and adheres to policies and procedures that demonstrate the intent required under this subparagraph; and
- (iii) the housing facility or community complies with rules issued by the Secretary for verification of occupancy, which shall--
  - (I) provide for verification by reliable surveys and affidavits; and
  - (II) include examples of the types of policies and procedures relevant to a determination of compliance with the requirement of clause (ii). Such surveys and affidavits shall be admissible in administrative and judicial proceedings for the purposes of such verification.

NOTE: <u>For senior developments, consideration should be given to selecting (c) above (occupancy persons of 55 years or older) which would allow for increased marketability of the development.</u>

TYPICAL HMFA FEES AND COSTS ASSOCIATED WITH THE TRANSACTION

Fees and Charges

Application Fee

Developers will be responsible for payment of a non-refundable application fee of $2,500 due at the time of the initial application.

For Preservation projects, if a project is currently in the HMFA's portfolio, the application fee is waived.

Commitment Fee

The Developer will be required to pay a commitment fee in an amount equal to one (1) percent of the estimated mortgage amount projected at mortgage commitment but not to exceed $50,000. This fee may be paid in cash or posting an unconditional and irrevocable letter of credit acceptable to the HMFA.

The commitment fee is refundable at the latter of the issuance of bonds or mortgage closing. In the event that the project does not proceed to mortgage and/or bond closing, the fee shall not be refunded.

Re-Commitment Fee (non-refundable)

A $2,500 re-commitment fee will be charged. This fee is due prior to the Board issuance of a re-commitment.

Pass Through Costs

The HMFA will order the appraisal, market study, and, Physical Needs Assessment.. The costs for the aforementioned reports will be passed through to the developer.

Cost of Bond Issuance

The cost of issuance is the Developer's allocable portion of the costs incurred by the HMFA for the issuance of bonds which include, but are not limited to, underwriter's fee, bond counsel's fee, rating agency's fee, printing costs, trustee and trustee's counsel fee, bond insurance premiums, and auditors' fee. The cost of issuance is included in the mortgage interest rate.

The costs associated with the issuance vary dependent upon the overall size of the bond issue and will be allocated based upon the percentage each participating loan represents to the total bonds issued.

Developers may reduce the interest rate by paying the cost of issuance out-of-pocket, which is presently anticipated to result in an approximate 15-basis point-reduction in rate. This election must be made two weeks prior to the date of the bond pricing. The payment of same must be made one week prior to bond pricing.

Negative Arbitrage Escrow

A negative arbitrage escrow will be created which represents the difference between the rate the HMFA pays on the bond and the rate realized by the HMFA on the investment of the bond proceeds. The payment of same must be made one week prior to bond pricing.

Financing Fees

Construction Servicing Fee

A 50 basis points servicing fee on the principal loan amount must be budgeted. This fee is incurred annually and billed monthly in equal installments throughout the anticipated construction term and is based on the original note amount.

Annual Servicing Fees

On all amortized debt, the HMFA servicing fee which is based on the original note amount shall be, at the option of the sponsor, either (a) zero points at loan closing and an annual fee of 65 basis points (55 basis points for projects paying the 2% tax credit allocation fee) or (b) 2 points at loan closing and an annual fee of 50 basis points (40 basis points for projects paying the 2% tax credit allocation fee).

Financing Fee on Non-Amortizing Debt

If the HMFA is providing tax-exempt financing through the provision of two first mortgage notes in order to meet the 50% aggregate basis test as referenced in the section entitled "Tax Exempt Bond Volume Tax Credit", then the servicing fee for the first note, shall be as determined in accordance with the above section on "Annual Servicing Fees" based on the original amount of the first note. The financing fee, for the non-amortizing second note, which is due at loan closing, is two points based upon the amount of the second note.

A financing fee of two points shall also be due on all other non-amortizing debt provided by the HMFA, including HMFA construction bridge loans. A construction service fee is incurred if non-amortizing debt is used during the construction period. In that case, a 50 basis point servicing fee is charged based upon the principal loan amount.

Sponsor's Predevelopment Loan

Reimbursement of Sponsor's predevelopment loan will be allowable at a rate of Prime plus two points, simple interest.

Processing and Review Fee

An additional processing and review fee of $2,000 will be charged at time of application, to any project sponsor, which seeks Agency financing to be secured by a leasehold mortgage or a condominium regime structure.